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Are Supreme Audit Institutions fit for purpose in the age of COVID-19 and beyond?

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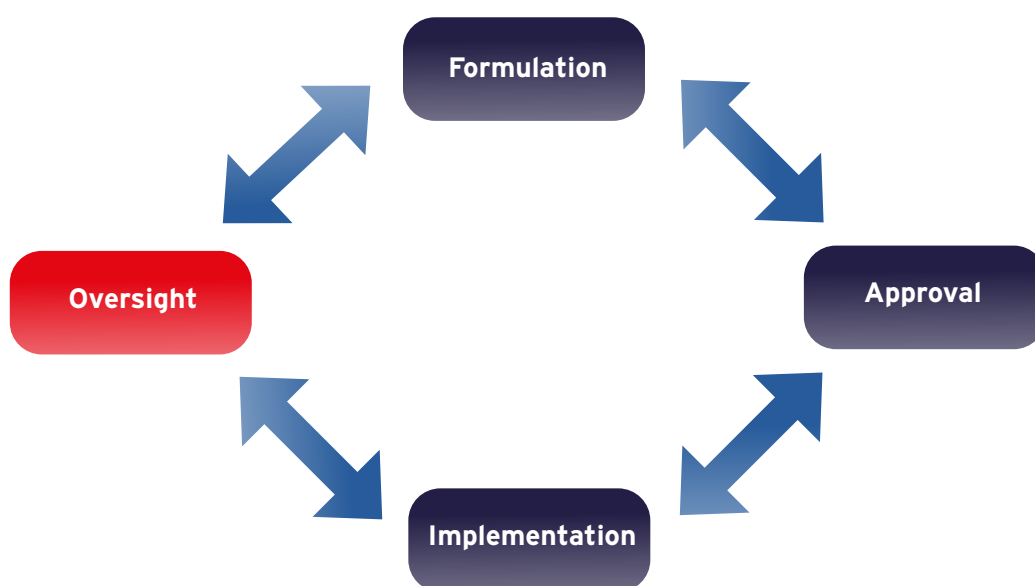
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Introduction

As part of Westminster Foundation for Democracy's (WFD) eight-part series on financial accountability, this brief focuses on the role of Supreme Audit Institutions (SAIs) and whether they are fit for purpose in the age of COVID-19 and beyond. This brief outlines how SAIs play an integral role during the *ex-post* oversight stage, as well as how SAIs can:

- contribute to the implementation of national priorities;
- increase their value-added role; and
- work with parliament and the executive branch to strengthen their value-added.



How are SAIs integral to the *ex-post* oversight stage?

As 'national watchdog agencies that audit government expenditure', SAIs are mandated to 'check if government spending is in line with the laws and policies adopted by parliament' and 'to provide an x-ray of the financial administration of the state and to ensure that public funds are spent efficiently'.¹

SAIs are an integral part of the fourth and final stage of the budget process. While government internal controls (including internal audit) are an integral part of the implementation phase, only SAIs provide independently verified *ex-post* information on government spending. Box 2 outlines the three main types of audit conducted by SAIs. Criteria for SAI independence is outlined in the Mexico Declaration on SAI Independence (2007).²

In countries following the Westminster tradition, parliaments scrutinise SAI reports, endorse and supplement SAI recommendations and monitor the government's implementation of these recommendations. Typically, the Public Accounts Committee (PAC) is assigned this *ex-post* scrutiny role.³

1. Agora Portal. 'SAIs Intro 1'. Online at <https://www.youtube.com/watch?v=4luMbredyi0>.

2. INTOSAI 'Mexico Declaration on SAI Independence'. INTOSAI P-10. 2019.

3. More information on Public Accounts Committees is provided in the WFD brief entitled 'A Critical Review of Public Accounts Committees' (Brief number 2 in the eight-part series on financial accountability), published September 2020.

How can SAIs contribute to the implementation of national priorities?

As countries grapple with COVID-19, climate change, the need for inclusive growth that benefits everyone - including vulnerable populations such as women - and the implementation of the sustainable development goals (SDGs), there is a growing consensus that the executive branch alone cannot solve all of these problems. As the Organisation for Economic Co-operation and Development (OECD) notes, 'governments have a need for objective and external views on policy formulation, implementation and evaluation', which should complement the government's own internal controls and evaluation capacity. SAIs 'contribute to a more robust evidence-base by complementing government-led evaluation with external assessments'.⁴ Yet, as the OECD also notes, 'SAIs have untapped potential to go beyond their traditional oversight role and contribute evidence for more informed policy-making'.⁵ So, how can SAIs contribute to the implementation of national priorities?

With respect to national implementation of SDGs, many SAIs are tracking the government's progress, monitoring implementation and identifying 'improvement opportunities across the full set of the SDGs'.⁶ Box 1 provides an example of a cooperative performance audit conducted by 73 SAIs on government preparedness to implement the SDGs.

Box 1: Adding value - a cooperative performance audit of SDG implementation

In July 2019, the International Organization of Supreme Audit Institutions (INTOSAI-IDI) released a report entitled 'Are Nations Prepared for Implementation of the 2030 Agenda? Supreme Audit Institutions' Insights and Recommendations'.⁷ The purpose of these cooperative audits was to 'urge national governments into action (on SDG implementation) if there wasn't any and provide constructive recommendations at an early stage'. To illustrate, one common insight was that budget systems needed to fully integrate costing for the implementation of the SDGs as well as translating national plans into budget allocations.⁸ This type of recommendation urges the executive branch to bring about systemic changes that will improve government performance over time.

The global COVID-19 crisis will likely compound the difficulty of governments around the world in achieving their SDG implementation plans as already sparse government resources are reassigned towards fighting COVID-19. SAIs may need to reallocate scarce resources used to audit implementation of the SDGs towards auditing government spending during the COVID-19 crisis, which in many cases will not follow normal procurement guidelines and where opportunities for misappropriation could be rife.

4. OECD. 'Supreme Audit Institutions and Good Governance: Oversight, Insight and Foresight'. OECD Public Governance Reviews. 2016. Online at: <https://doi.org/10.1787/9789264263871-en>.

5. OECD. 'External Audit - Supreme Audit Institutions'. Online at: <https://www.oecd.org/gov/external-audit-supreme-audit-institutions.htm>.

6. <https://www.idi.no/en/idi-cpd/auditing-sustainable-development-goals-programme/sdgs-audit-publication>

7. INTOSAI IDI. 'Are Nations Prepared for Implementation of the 2030 Agenda? Supreme Audit Institutions' Insights and Recommendations'. July 2019. Online at: <https://www.idi.no/en/e-library/cdp/auditing-sustainable-development-goals-programme/949-are-nations-prepared-for-implementation-of-the-2030-agenda/file>

8. Ibid.

How can the value-added of SAIs be increased?

When the COVID-19 crisis is finally behind us, it will be more important than ever for both government and non-government institutions alike to support implementation of national priorities. The key question is whether SAIs are well poised to support this effort. To become fit for purpose, SAIs may want to take the following into consideration:

A) Rebalance audit portfolio. Currently, SAIs in low- and middle-income countries conduct mostly financial and compliance audits at the expense of performance audit. The fact that many SAIs have a legal or constitutional requirement to submit the first two types, as well as an annual due date for their submission, means that they are forced to assign priority to them over performance audit.

The Kenyan Constitution (2010), for example, requires that the Auditor General perform an annual audit for:

- (a) the accounts of the national and county governments;
- (b) the accounts of all funds and authorities of the national and county governments;
- (c) the accounts of all courts; and
- (d) the accounts of every commission and independent office established by this Constitution.

The requirement to cover all of the accounts does not permit SAIs to adopt a risk-based approach that would help with the efficient allocation of resources. According to a 2017 stocktaking report, only 62% of 'developing countries'⁹ are meeting a 75% threshold for coverage of financial statements, suggesting that SAIs will require additional resources to not only meet but to surpass this standard. Similarly, for compliance audits, only 58% of SAIs in 'developing countries' were selecting their compliance audits with a criteria based on risk.¹⁰

The review of individual cases of non-compliance tends to frustrate parliamentarians. There may be hundreds of examples of the same type of lack of compliance across numerous ministries, departments and agencies (MDAs). Examining these breaches individually does little to address the root cause resulting in the same issues resurfacing year after year. Audit reports that aggregate findings of non-compliance can be more useful to parliamentarians because they provide a big picture of where the systemic weaknesses are.

Increasingly, SAIs are 'moving (away) from a focus on government compliance with financial legislation and budget appropriations, to an emphasis on value for money and government performance in managing public resources and implementing public policies'.¹¹ Because of this new focus, SAIs are transforming into advisers rather than controllers of government. The advice comes in the form of a value-for-money or performance audit, which examines the extent to which government is implementing programmes with due regard to economy, efficiency and effectiveness. Performance audits tell a story, often about the performance of government in delivering services, that parliamentarians can understand and relate to. As a result, most of the

9. According to the Global SAI Stocktaking Report, 'developing countries' are categorised "as the official INTOSAI (or INTOSAI regional body) member SAIs from countries and territories on the Development Assistance Committee of the Organisation for Economic Co-operation and Development (OECD-DAC) list of official development assistance (ODA) recipients. These are further classified as: 'Low Income Countries' corresponding to Least Developed Countries and Other Low Income Countries; 'Lower Middle Income Countries'; and, 'Upper-Middle Income Countries'. See INTOSAI IDI 'Global SAI Stocktaking report 2017'. 2017.

10. Additionally, to meet this benchmark, at least 60% (by value) of the audited entities within the SAI's mandate needed to be subject to a compliance audit in the last audit year.

11. Carlos Santiso. 'Why Budget Accountability Fails? The Elusive Link Between Parliaments and Audit Agencies in the Oversight of the Budget Process', p. 604.

hearings held by PACs in many high-income countries, including the United Kingdom and Canada, are focused mostly on performance audit. Those countries made their own transition away from financial and compliance audit in the 1970s. See Box 3.

Unfortunately, in most low- and medium-income countries, the number of such performance audits is still negligible, when compared with the high level of engagement of SAIs in the realm of financial statement and compliance audit. In these cases, SAIs are dedicating limited resources to performance audit.

Nonetheless, most SAIs have recognised the importance of conducting more performance audits and many have in fact increased their performance audit capacity. Still, the plans to incorporate performance audit for most SAIs are incremental, not transformational. For example, AFROSAI-E, the African Regional Association of SAIs (covering the English-speaking countries in Africa), suggests that at least ten performance auditors would be required to develop 'a large enough specialised performance audit unit (able) to sustain performance audit activities on a continuous basis and to develop a performance audit culture'. Expectations are that such a unit would produce at least three performance audit reports per year.¹² However, according to INTOSAI's 2017 Stocktaking Report, only 46% of 'developing countries' responding had managed to meet this benchmark. A number of regions (not disaggregated by income status) were falling below this benchmark, with none of the Francophone African SAIs and only 20% of Caribbean SAIs achieving this goal.¹³

Box 2: Defining the three main types of audit

The International Association of Supreme Audit Institutions (INTOSAI) defines the three key types of audit as follows:¹⁴

Financial audit focuses on determining whether an entity's financial information is presented in accordance with the applicable financial reporting and regulatory framework. This is accomplished by obtaining sufficient and appropriate audit evidence to enable the auditor to express an opinion as to whether the financial information is free from material misstatement due to fraud or error.

Compliance auditing is performed by assessing whether activities, financial transactions and information are, in all material respects, in compliance with the authorities which govern the audited entity. These authorities may include rules, laws and regulations, budgetary resolutions, policy, established codes, agreed terms or the general principles governing sound public sector financial management and the conduct of public officials.

Performance audit focuses on whether interventions, programmes and institutions are performing in accordance with the principles of economy, efficiency and effectiveness and whether there is room for improvement. Performance is examined against suitable criteria, and the causes of deviations from those criteria or other problems are analysed. The aim is to answer key audit questions and to provide recommendations for improvement. Compliance audit focuses on whether a particular subject matter is in compliance with authorities identified as criteria.

12. Only at the 'managed level' are SAIs expected to utilise at least 40% of its audit staff for performance audits. This rises to 50% for the 'optimised level'. See AFROSAI-E. 'Template Performance Audit Manual'. November 2016, p. 21.

13. INTOSAI IDI. 'Global SAI Stocktaking report 2017'. Annex Volume. 2017.

14. INTOSAI. 'Fundamental Principles of Public-Sector Auditing'. Endorsement Version. No date.

B) Adopt a more holistic approach. For SAIs to become more analytical in their work, financial and compliance auditors need to be trained to take a more holistic approach that goes beyond the auditing of individual transactions. For example, annual reports need to be supported by an executive summary that provides parliament with an overview of the systemic weaknesses found in financial statements and compliance audits, together with an analysis of the extent to which these weaknesses are being addressed year over year.¹⁵

The striking of multidisciplinary audit teams (containing forensic audit and performance audit specialists along with compliance auditors, for example) can provide 'a diversified look at a problem' and enhance the capacity of SAIs to produce more profound audit reports that provide insightful audit findings beyond simple compliance issues.¹⁶ The three audit types can also be combined 'to enhance audit opinion on achievement of national objectives or SDGs. Thus, some audits might be combined, with an emphasis on performance audit and an integrated approach aiming to arrive at convincing recommendations'.¹⁷

C) Reflect on societal impact. SAIs need to be more proactive in obtaining feedback from key stakeholders and parliament on the value-added of their audit reports. SAI audit products need to be useful to parliament in the broader societal context, and add value to governments by supporting ways to track progress in achieving important national priorities and providing feedback to inform parliament and the government. AFROSAI-E suggests that a highly 'developed' SAI should be 'able to scan the environment and position itself and by that use the resources in the most proactive and value adding way'.¹⁸ This practice should not be confined to the most developed SAIs. SAIs need to be reflecting regularly on their societal impact.

Box 3: Transition to performance audit at the Office of the Auditor General of Canada

In the 1970s, in Canada, the Office of the Auditor General (OAG) of Canada led the way in shepherding new legislation that strengthened its independence and mandated the Office to conduct value for money (now referred to as performance) auditing. Similar measures were adopted by the UK and Australia. The motivation was for the external auditor to take on the role of management consultant to government rather than acting exclusively as an adversarial compliance auditor. This does not mean that the Office lost its independence. To the contrary, the new audit Act allowed the OAG to hire and classify its own staff, independent of the Public Service Commission.

The transformation of SAIs in the 1970s did not happen in a vacuum. In Canada, in the previous decade, the government had begun migrating toward a new Expenditure Management System (EMS). This system featured the development of an early form of results-based budgeting, together with a decentralisation of management practices to line departments, which in turn necessitated the development of strong internal control systems within government.¹⁹

15. OECD - SIGMA 'Developing Effective Working Relationships Between Supreme Audit Institutions and Parliaments'. SIGMA PAPER No. 54; 1.2.2, p. 13. Online at:

http://sigmaweb.org/publications/Supreme_audit-institutions-and-parliaments-SIGMA-Paper-No.%2054.pdf.

16. INCOSAI. 'Discussion paper on Theme II'. XXIII INCOSAI The Role of the Supreme Audit Institutions in the Achievement of the National Priorities and Goals. July 2019.

17. INCOSAI. 'Discussion paper on Theme II'. XXIII INCOSAI The Role of the Supreme Audit Institutions in the Achievement of the National Priorities and Goals. July 2019.

18. AFROSAI-E's Institutional Capacity Building Model has five levels of SAI development. The most developed SAIs are referred to as 'optimized'. See AFROSAI-E. 'Institutional Capacity Building Framework'. November 2015.

19. Geoff Dubrow. 'The Introduction of Value-For-Money-Auditing in Canada and the Link to Broader Changes in Planning and Expenditure Management'. Parliamentary Centre, 2004.

How can SAIs work with parliament and the executive branch to strengthen their value-added?

In our hyper-political world, governments have often been slow to realise that SAIs can help them track implementation of national priorities, particularly by identifying systematic weaknesses in public administration that end up blocking progress. Until this fact is acknowledged, governments will likely continue to be reticent about getting SAIs on board. Lack of government support may help to explain why SAIs are often waiting an inordinate amount of time to have their performance audits tabled for review by parliament.²⁰ This fact may also explain why, in many countries, SAIs face political interference, which is exacerbated by a lack of SAI independence from the executive branch.²¹

COVID-19 has demonstrated systemic weaknesses in political and economic systems. The reality is that for governments to achieve their policy goals, SAIs are needed to provide independently verified analysis about the shortcomings and impediments in public administration. To affect this transformation, governments, SAIs and the international community will need to think beyond incremental change and embrace comprehensive and fundamental changes. Here are some ways to accomplish that goal:

First, SAIs, parliaments and governments need to collaborate to more clearly understand and articulate how SAI resources can best serve the national interest. In some cases, this will mean an eventual legal or constitutional change in SAI mandates and a shift of resources away from financial and compliance auditing. Parliamentarians need to clearly articulate their desire for more high-level information that outlines the root cause(s) of deficiencies identified by the SAI. PACs and other oversight committees should play a role in formally requesting that such high-level summaries accompany SAI reports.

Second, PFM practices in most low- and middle-income countries are a major impediment to effective SAI performance. In particular, government internal controls (particularly internal audit) remain weak, forcing the external auditors to, for all intents and purposes, perform the internal audit role as well. Stronger internal control systems would allow SAIs to pivot to a risk-based approach to compliance, based on testing of internal controls, leaving room for increased performance auditing and for compliance audits that contain more holistic findings. It is noteworthy, for example, that in Ethiopia, where the internal audit function has an unusually strong presence, the Office of the Federal Auditor General (OFAG) carries out approximately two dozen performance audits annually, which far exceeds the aforementioned AFROSAI-E target.²²

Third, most contentious and difficult to operationalise is the notion that SAI independence, while fundamental, cannot be an excuse to maintain the status quo. Institutional resistance to change is not a new concept, nor is it limited to SAIs. While SAIs need to protect and even strengthen the tenets of SAI independence going forward,²³ this should not be done to the detriment of SAIs becoming more agile. SAIs need to be open to dialogue with parliament and the executive branch on changing their mandate, while at the same time ensuring that independence is at least respected if not enhanced.

20. AFROSAI-E. '2018 State of the Region ICBF Self-Assessment Report'. 2019. Online at: <https://afrosai-e.org.za/wp-content/uploads/2019/07/2018-State-of-the-Region-ICBF-Self-Assessment-Report.pdf>

21. For a summary of the core principles on SAI independence, based on the Mexico Declaration, see the INTOSAI Framework of Professional Pronouncements. "INTOSAI-P - 10 - Mexico Declaration on SAI Independence". Online at: <https://www.issai.org/pronouncements/intosai-p-10-mexico-declaration-on-sai-independence/>.

22. Ethiopia (Federal Government) Public Expenditure and Financial Accountability (PEFA) Assessment. November 2019.

23. The principles of SAI independence are outlined in the 'Mexico Declaration on SAI Independence'. Online at: https://afrosai-e.org.za/wp-content/uploads/2019/04/ISSAI-10 -Mexico-Declaration-on-SAI-Independence1_00.pdf

Finally, donors need to treat the PFM system in a more holistic manner, rather than developing stand-alone 'parliamentary development' or 'SAI strengthening' programmes. PFM reform programmes need to include an SAI component and SAIs need to be invited to the table during the design phase, so that SAI feedback can inform programme design. SAIs and donors need to be more vocal about the need for governments to strengthen internal controls and internal audit so that SAIs can gravitate away from auditing individual transactions and focus on more systemic issues.

Conclusion



SAIs are apex-level national external audit offices that are the mainstay of *ex-post* oversight. Particularly (but not exclusively) in countries following the Westminster system, SAIs are dependent on parliament to act on their findings by reviewing SAI reports and recommendations and tracking their implementation.

Even prior to the COVID-19 crisis, SAIs were inundated by their own (often) statutory requirements to audit, at a minimum, all central government accounts on an annual basis. The time and resources to conduct root cause analysis and provide analysis of more systemic issues has been limited.

The COVID-19 crisis has diverted significant yet scarce resources away from SAIs to examine the implementation of national priorities, including the implementation of climate change plans. The incremental change that has characterised progress in most low- and middle-income countries will likely not be sufficient and will not allow SAIs to play the strategic role that is very much required of them.

In order to be fit for purpose for 2020 and beyond, SAIs will need to rebalance their audit portfolio so that more performance audits are being performed, and PFM reform will need to result in improved internal audit capacity so that SAIs can focus on the higher-level issues, as they do in many high-income countries. A more holistic approach to audit, characterised by financial and compliance auditors looking for root cause and by multidisciplinary teams, will need to prevail.

Closing with a quote from Harvard management guru Peter Drucker, 'the greatest danger in times of turbulence is not the turbulence - it is to act with yesterday's logic'. The current laws, mandates and personnel structure that underpin the operation of most low- and middle-income country SAIs will not be sufficient to address the monumental challenges that governments are facing in 2020 and beyond. Change will not be easy, but the transformation is essential.



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